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PRIVATE PENSION FUNDS CHALLENGE FOR THE PENSION SYSTEM REFORM IN ALBANIA

Abstract

The object of this study is the analysis of private pension funds and the challenges for the reform of the pension system in Albania after the fall of the communist system, the progress of its most important indicators, the reforms undertaken in the system of private pension funds. Of course, after this analysis naturally emerging problems and further reforms that need to be made to the system in order to maintain its financial sustainability, good administration, etc. The Private Pension Fund is a saving tool designed for additional income when retiring. Among the main factors affecting pension funds are the legal and regulatory framework, prudent investment policies, time span (investment time extension) and public transparency and credibility.

Key words: private pension funds, pensions, insurance, social security, health insurance, penitentiary schemes, fixed-term pension, permanent-term pension

Entry

Recent years have witnessed an intensive retirement effort in many parts of the world, which often involved a widespread use of private sector managed pension programs. Under these conditions, the need to compare the development of programs and experiences between different countries is very important for policy makers, supervisory authorities, and private sector participants.

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Private pension plans are playing a very important role in securing retirement income, and investment in pension assets will have an ever-increasing impact on financial markets in many countries around the world in the future as well.

Pension funds are considered as large businesses and are important for employers, employees, governments and societies in general.

Social security has evolved in parallel with the economic development of the entire society. In a sense, it can be said that their birth is related to the industrial revolution, with the emergence and consolidation of the modern state and the middle class itself. The level of solving such problems, such as lack of old age, sickness, invalidity etc., is conditioned not only by the way of life of employees, the unemployed, those who have not reached the age of employment but also from the demographic structure, the interest of individuals to solve their problems, etc.

But, referring to the historical social security developments, it is noticed that even the best solutions offered, always remain as temporary alternatives. The provisional nature of these solutions is determined in every case by general economic developments, but on the other hand, for several decades, almost all governments of countries that respect democratic standards respect the obligation to guarantee the rights of the individual, where the right to the benefit of social security, is one of the fundamental principles. In this context, the reform of pension systems, whether full or partial, has a considerable place in the electoral programs of each government, trying to make the individuals more sensitive about the economic program being offered.

1. Private pension systems

Pension funds and their form of occurrence.

Private Pension Funds are financial institutions with important effects in two main directions, first in the social one, as an instrument through which individuals can save money for their retirement and secondly, as a very important factor in the capital markets, so the Private Pension Fund is a savings vehicle designed for extra income when they retire. The main task of private pension institutes is to accumulate contributions and invest with maximum security, while the purpose of private pension insurance is to provide: a) early retirement pensions. b) Additional old age, invalidity and family pensions, over those provided by compulsory social security scheme against paid contributions and realized earnings.

In many developed countries in the world, employers are encouraged by governments to create private pension funds in addition to social security contributions, not just to provide other income sources for their employees at the time of retirement but also to promote savings at the national level.

Pension funds include a wide range of savings ranges from social security schemes to voluntary individual contributions schemes or profit-based schemes within the company. Contribute-based schemes are those schemes in which the employee and / or the employer set a fixed amount each month mainly at the time of the payout; Benefit-based schemes within the company at the time of old-age guarantee the employee a certain periodic benefit in the retirement period. Adoption of Law No.7943, dated 01.06.1995 “On Supplementary Pensions and Private Pension Institutions (and amendments made to the law No. 8393, dated 2.09.1998 “), as well as the completion of the institutional infrastructure of the regulatory framework, have created the possibility of licensing private supplementary pensions institutes, laying the groundwork for a new alternative, which will operate in parallel with the scheme current state social insurance. This enables every individual to invest safely by creating a stable economic base for the retirement period.

Development of private pension scheme in Albania

Pension fund management companies have not existed and therefore neither the services provided by this service. The same situation appears in other former communist countries.

With the fall of the communist system and changes in political platforms in countries that had experienced it before, the economy focused on free market operations. At this time, the broader presentation and the development of financial services became a necessity for many countries. The compromises between the successful models applied in the developed countries and the needs that appear in countries like Albania, in most cases, proved to be a necessity for the growth of the welfare of the population.

The financial services sector has never been known before in Albania, with the exception of some limited banking sector operations. At any moment, the government exercised full control and in no case did it leave room for any other initiative in this regard. It has always been the duty of the state, the determination of wages and pensions, which in general have been at very low levels, and furthermore it was noted that the ratio between salaries and wage categories has never been higher than 1: 2.

In the case of Albania, the question is coherent: “Why is it required a 20

year period to create service sectors of this nature”? The answer to this question is closely related to the difficulties the country faced during the transition. Judging from this point of view, what makes the situation more difficult, apart from the above phenomenon, is the attempt to influence the change of mindset and mentality. As noted, this is one of the biggest challenges faced by any government that has come to power over the last 20 years.

The insurance sector and its development in recent years is a good illustration of the comments made above.

Pension Companies are controlled and monitored by the Financial Supervisory Authority, a public institution under the authority of Parliament, established by Law No. 9572, dated 3/07/2006 “On the Financial Supervisory Authority”, which plays the role of the regulator for the functioning of the private pension scheme

Entry into force of Law no. 10 197, dated 10.12.2009, “On Voluntary Pension Funds”, has brought about the improvement of the legal basis and the adoption of new subordinate legal acts in implementation of this law. This law made it possible to adapt to international standards and directives. European pension fund for the third pillar of private voluntary pension contributions is certain.

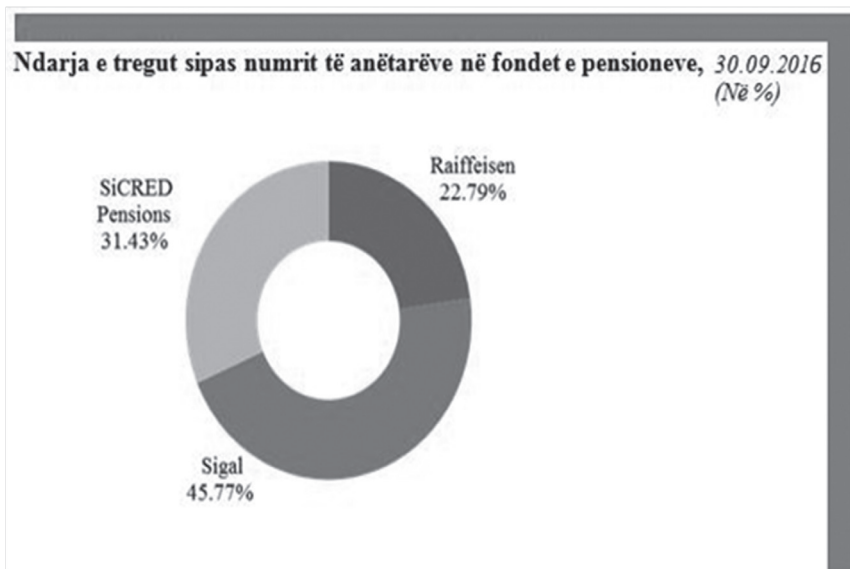
1. The law aims to improve the existing system of voluntary private pension in Albania with expected impacts:
2. Facilitate long-term social costs by stimulating citizens to save privately and voluntarily to increase their retirement;

Increasing the level of population saving and increasing long-term investments in the country.

Based on the contribution rate, the timeframe for participation in the supplementary pension scheme, the selected pension plan and the investment return of the funds also determines the benefit that the adherents will receive in the form of a pension. At present, there are three voluntary pension fund management companies operating in the market, respectively, which are under the management of a pension fund.

Companies operating in the private pension market operate:

- Raiffeisen
- Sigal
- SicredPensions



Voluntary Private Voluntary Pensions Market

Significant development during 2011 in the voluntary private pension market has been the licensing of operators expected to play an important role in maturing this market, further increasing public confidence in the investment of funds in the private voluntary pension scheme. An important aspect in AFSA's work, after the entry into force of the new Law no. 10197, dated 10.12.2009 "On Voluntary Pension Funds", has been the further completion of the legal framework. The new scheme of the organization and operation of private voluntary pensions, sanctioned in the new law, constitutes a novelty for the Albanian financial market. In January 2011, a licensed operator developed the activity according to new requirements, while during the year were licensed and 2 other operators.

Licensing according to European standards of new operators in this market is expected to play an important role in its maturity, further increasing public confidence in the investment of funds in the private voluntary pension scheme. Furthermore, the inclusion of tax incentives in this law, which aim to make the private pension scheme more attractive to contributors and employers. The analysis of data on the private voluntary private pension market until 30.09.2016 shows a total under management asset of 837.09 million lek and net investment income of about 6.01 million lek. The average value of the monthly contribution paid to the voluntary private pension funds during 2016 ranged from 2,000 ALL

to 13,600 ALL depending on the fund, while the number of active members or members who have made at least one contribution is 5.275 6,295 total members that are registered until 31 December 2016 in these funds.

Field of activity of new private pension institutes

Today, six minimum conditions are being sought to enable the activity of private pension funds to be applied in developing countries, including Albania

- The low level of average income (compared to the American system where the minimum income limit is considered \$ 2000 per capita) requires a higher level of demand in the field of economic services;
- Acceptable macroeconomic policies, which create a suitable and long-term environment for the functioning of financial mechanisms;
- The normal functioning of nuclear financial institutions (banks and institutions providing guardianship services), as well as government engagement for economic development;
- Open capital accounts to increase investment diversity and at the same time reduce risk of losses;
- Complete legal platform;
- Full transparency vis-à-vis the general public.

Based on some business plan calculations, two out of three companies operating in Albania are seen as an indispensable need for an initial investment amounting to a total of nearly € 1 million extended over a 2-3 year period. For the sake of being “measured” in the way of calculations, and to guarantee the fact that capital will be available to the company, is foreseen as an essential condition at the outset of the activity and at the first stages of development to be destined an initial capital for the company in the total amount of 1.5 to 1.8 million Euros, which must, in any case be guaranteed by the shareholders, thus providing a sufficient amount , sufficient to cover the tolerances of which is foreseen, if need arises.

The way of investment

Retirement pension with defined benefit time

A defined-benefit pension is the type of pension in which the contributor determines a period of time during which he will benefit from supplementary pension.

Example: One person at the age of 35 thinks he will save 5,000 ALL a month for the next 20 years. This person has the opportunity to choose the timeframe for how long he or she wants to benefit from these savings. He can choose to get the full amount at the end of 20 years of saving (even earlier if he wants it). By taking INSTAT data for life expectancy, where life expectancy for men of 55 years is about 20 years, this person chooses to receive monthly benefits in 20 years. Then we would have:

Time Coverage	Monthly paid contribution	Monthly benefit for 20 years
20 years	5,000 ALL	13,600 ALL

Meanwhile, if the adherent is separated from his or her life before reaching his entire fund, through the Family Pension, the remainder withdraws the person designated by him in the contract, and if no contract is specified, then inheritance laws are used.

Permanent Pension (ANNUITY)

A permanent-term pension is the type of pension in which the contributor receives supplementary pension throughout his / her life from the moment of the beginning of the pension.

Assume that the person above is a woman. Due to the uncertainty surrounding the life and the fear that he may live longer than the time it provides for retirement benefits, she may decide to sign a permanent term supplementary pension contract. So, in our case, make contributions for 20 years, up to the age of 55 and then benefit a permanent pension.

How does this permanent pension work?

For this, computational actions are a bit more complicated. As a basis for calculations, the average life expectancy determined by INSTAT at the moment of retirement for men and women by age groups will be taken. For a woman at the age of 55, the average life expectancy is 25 years. The insurance company calculates that you receive a permanent pension using as a basis this timeframe, and concretely in our case would be 12,000 ALL per month. Even if the person lives for more than 25 years, the insurance company guarantees to give a monthly pension of 12,000 ALL each month.

Meanwhile, if the person is divorced before withdrawing all the funds created by him, the applied family pension will be different from the one above.

For calculation purposes, the life expectancy index obtained as a basis is divided into two equal parts. If the contributor dies during the first half, until the end of the first half, the family will benefit 90% of the monthly pension. For the second half the benefit rate is 78% of the monthly pension.

If the family wants to receive an immediate amount of the family pension, when the contributor dies during the first part of the index, the family will benefit 95% of the remaining principal. If he dies in the second half, the family will benefit 90 percent of the remaining principal.

Benefits from private pension schemes.

Private pension schemes provide 3 types of benefits:

- a) Additional benefits on old-age, invalidity and family pensions in addition to those benefits deriving from the compulsory insurance scheme.
- b) Long-term benefits, which are determined by seniority at work, enabling early retirement and disconnection from the compulsory insurance scheme.
- c) Other additional benefits in value or in kind, as a result of the fund's investment profits.

The Supplementary Pension Fund provides for compensation of income or additional income in cases of disconnection of employment prior to the age of a compulsory insurance pension, when financial relationships are interrupted for various reasons and have been completed over 180 historical months as well as to obtain additional income over those provided by the mandatory state scheme. Specifically, supplementary old-age pension, old-age benefits, early retirement pensions, invalidity pensions, family pensions, disbursements and other benefits derived from the contract and that are foreseen in the fund's pension regulation. The special retirement provisions are as follows:

The supplementary old-age pension is provided by men and women after the age of the compulsory insurance law, when they have insurance periods of not less than 60 months. Under the compulsory social security scheme, the age of retirement benefits is at least 62 aged for men and 57 for women or for a maximum of 65 and 60 years.

Early retirement benefits benefit men after reaching the age of 45 and women after reaching the age of 40 when they have insurance periods of no less than 60 months and when they do not carry out economic activity.

Early retirement benefits the participants when they do not carry out economic activity and have IFP periods of insurance not less than 180 months.

The insured who becomes completely disabled receives a disability pension when benefiting from it and the compulsory insurance scheme and has completed 60 months of insurance. The amount of the invalidity pension shall be calculated as for the old-age pensions. The persons defined or in the caretaking of the insured person who dies and who has completed the minimum insurance period of 5 years are entitled to a family pension.

Settlements and other benefits, immediate payment of the account position in the form of settlements are made when the insured has completed his insurance in supplementary pensions, has paid contributions for at least 12 calendar months, has not benefited from the right for his pension, his contributions have not been transferred to another pension institute.

The reasons that enable development in Albania

The three main motives behind the development of such a direction at this stage of the country's development are now clear.

1. As in other developing countries, where the birth rate has fallen sharply in the last decade, Albania is becoming a witness to this phenomenon. This phenomenon will definitely bring consequences for future generations by significantly reducing the number of contributors.

2. Today's legal definitions for the method of distributing the amount of pensions to those who have reached the age of 60/65, which have a time limit of about 35 years, are becoming more difficult to apply. This is seen in connection with the demographic composition that the country has nowadays. For a developing economy, where unemployment problems are high and with a very high percentage of emigration, these circumstances lead to a significant reduction in the total number of contributors. Also the low amount of collected contributions comes as a result of the fact that subjects that are currently in business relations have "speculated" with the mass of contributions during these 20 years of transition. The consequences of the above factors make it almost impossible to obtain a full pension plan for those who regularly make regular contributions. Situated under these conditions, many individuals, aware of the reality they will face in the future, are seeing other possible alternatives through which they will be able to provide sufficient income for the retirement period.

3. The current state scheme, even in the future, will remain limited to low pension payments. The current pension rate is at 36% - 38% of the amount of contributions paid out in the last 10 years of work, while no indexation has been made to offset the current rate of economic inflation in the country.

Albanian market assessed as a very favorable opportunity

The Albanian market is still untapped. The company's focus is mainly on these categories as potential customers:

1) Large companies such as telephone services, universities, OSHEE, oil and gas companies and self-employed. It is alleged that such high-paying companies will exhibit interest to include in such pension schemes and will create an initial pool for their employees to invest part of their income.

2) International institutions and non-governmental organizations, the financial services sector (banks and insurance companies), judicial assistance offices (private professional studios), business associations and other businesses of this nature, as well as individuals / employees of the state administration .

3) Key position personnel in companies where the average payout level is relatively low. Inclusion of this category into such private pension schemes is considered to be a kind of incentive for them.

Conclusions

It is clear now that Albania and many other countries of the world have entered the irreversible path of reform of the pension system, but are we really in the way and in the proper way of implementing these reforms?

The economic, social and political conditions make Albania, a country similar to other Eastern European and developing countries, as well as unique in many aspects of life and the way they perceive it. Of course, considerable steps have been made towards development, but this development has carried a not-so-small transition cost and has left a bitter taste to a large number of Albanians.

Private pension plans, a new and interesting alternative, are still being seen with much skepticism by the wider population, whose first impact, reminds them of pyramid schemes. This comes not only because of the little information they have, nor the ignorance of the legal regulation and the state control over the pension companies, but also of the lack of fiscal stimulus that the state itself should initiate.

Likewise, with increasing concerns about the reduction of pension benefits and the effect that the current crisis in the pension system has on public awareness, managing private plans does not have to be at a more critical stage than this, and the pressure on those responsible for private management are increasingly growing.

Lack of trust in management companies is also due to the fact that these

companies are still new, as soon as they have entered the market and as such have not yet shown themselves as successful.

Even the legal aspect has in itself shortcomings, which have led to the necessity of a full review of the law itself, which is likely to be done within this year.

Fiscal incentives. One of the main shortcomings of the current legislation is that it determines the taxation of contributions for pensions rather than benefits, which in the first place is the opposite of what the whole world applies in practice, and secondly, this conception reduces the competitive advantage of private pension companies to other money-laundering financial institutions.

Another disadvantage of the success of this new system in the Albanian market is that it is still not considered sustainable and attractive by powerful investors, although in itself this market is a significant part of the financial markets of each economy. state for the protection of domestic capital. The fact that the financial markets in Albania are in the phase of the newborn makes for a period of one to two years, for private pension funds do not have enough investment space. But when this market is opened up to internationalization, domestic companies may be at risk of aggressive competition from international companies in this area. This raises the need for state support, either by setting legal limits for investing most of the capital on domestic resources, but also by setting some temporary ceiling limits for the capital that can invest a foreign company

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